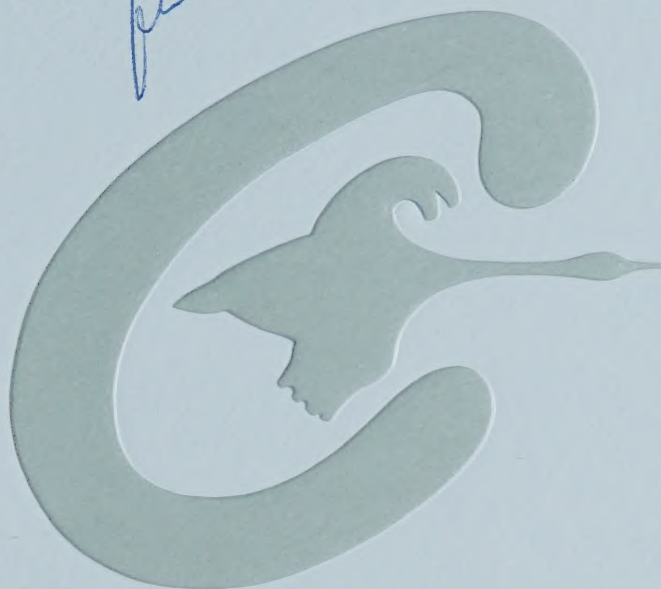


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~~Mr. Scott~~
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COLUMBIA CELLULOSE
COMPANY, LIMITED
ANNUAL REPORT 1964



COLUMBIA CELLULOSE COMPANY, LIMITED **ANNUAL REPORT** 1964

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COLUMBIA CELLULOSE COMPANY, LIMITED

MUtual 4-8311

1030 WEST GEORGIA STREET, VANCOUVER 5, B.C.

February 10, 1965

TO THE SHAREHOLDERS

The annual report of the directors, the financial statements for the year 1964 and the auditors' report thereon are set out on the following pages.

The net profit for the year amounted to \$4,077,378, equivalent to 50 cents per common share, after allowing \$6,671,379 for depreciation, amortization and depletion of fixed assets, and \$3,980,000 as provision for taxes on income.

The increase in the pre-tax profits to \$8,057,378 from \$7,369,458 reflects the continuing improvement in production and sales at the Celgar pulp mill, the high level of efficiency of the Celgar sawmill, and improved prices for our products. Delays encountered in expanding the Prince Rupert mill prevented the company from realizing the benefits of this project in 1964, but increased production will be available in 1965.

Markets for the products of the two pulp mills have been strong throughout the year and hold promise of continuing strength in 1965. Both mills ran at capacity with sales of all grades being limited only by availability of product. Despite increased production facilities available in 1965, production is again expected to be the limiting factor.

The Celgar Lumber Division operated on a three-shift basis for the full year. North American lumber markets opened the year at an unnaturally high level and showed a slow but steady decline from April until year end. Average prices for lumber for the year were almost identical with those of the previous year.

During the year the Skeena Kraft project was initiated. This 750-ton a day mill, scheduled to be in production early in 1967, is designed to serve as the basis for a major expansion of sales and profits.

During the first month of 1965 British Columbia has suffered the most severe weather conditions in many years. This has seriously hampered all operations of the company. However, with strong markets for our products, higher prices for sulphate and sulphite pulps and increased production facilities, the company looks forward to 1965 with confidence.

On behalf of the Board,

M. W. Mackenzie,
Chairman.

Paul M. Marshall,
President.

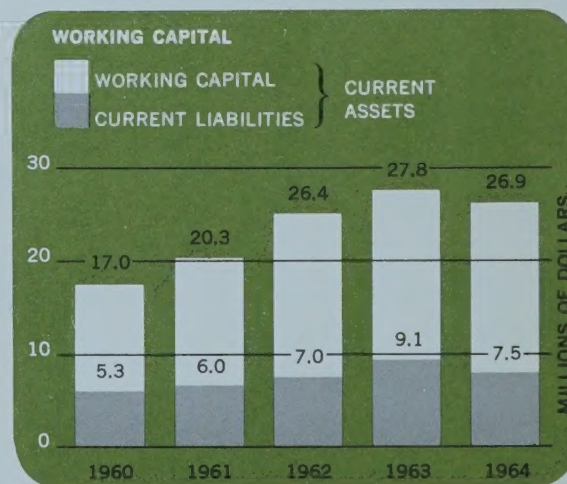
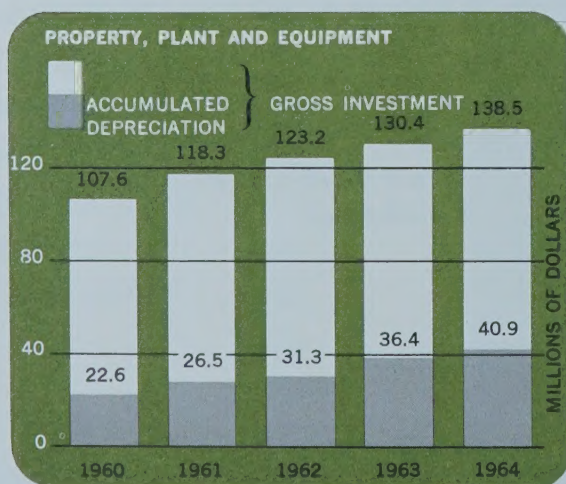
FINANCIAL RESULTS AND CHANGES

Net sales for the year amounted to \$62,347,417, an increase of 10% over 1963, resulting in operating profit before interest and non-cash charges of \$18,652,429 compared with \$17,431,397 in the previous year.

Depreciation, amortization and depletion, calculated on the same basis as in previous years, amounted to \$6,671,379 compared with \$6,244,338 in 1963. Provision for income taxes rose from \$3,590,000 to \$3,980,000 being approximately the maximum rate of 50%.

The net profit for the year stood at \$4,077,378 compared with \$3,779,458 in the previous year. This is equivalent to 50 cents per common share, an increase of 10% over the 45 cents per share recorded in 1963.

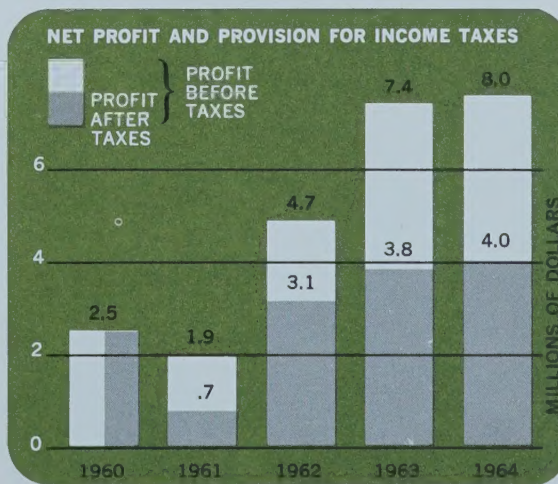
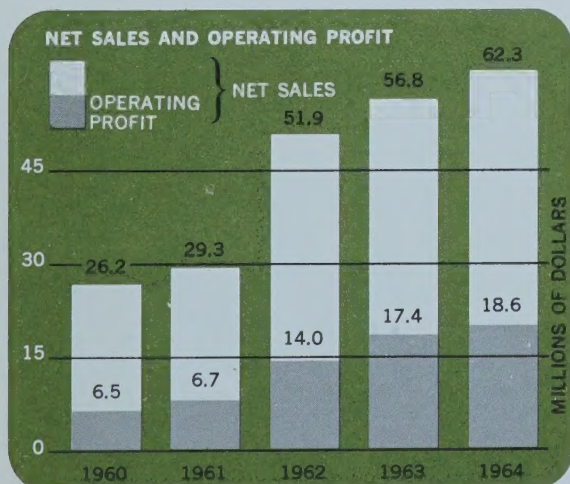
Cash generated during the year amounted to \$12,875,757, an increase of \$1,191,961 over the previous year. Of this, \$9,649,303 was used on capital expenditures designed to increase capacity of the mills and to reduce operating costs, and \$585,574 was used to cover preliminary expenses of the Skeena Kraft project. An additional \$3,426,912 was absorbed by changes in working capital resulting from the higher sales and reduction of current liabilities. \$1,480,761 was paid out in dividends on common shares. The net result of these transactions was a reduction of cash and equivalent from \$6,898,629 to \$4,274,970.



FINANCIAL SUMMARY AND REVIEW

(in thousands of dollars)

	1964	1963	1962	1961	1960
Net sales.....	\$ 62,347	\$ 56,768	\$ 51,907	\$ 29,305	\$ 26,223
Profit on operations before interest, depletion and amortization.....	18,652	17,431	14,048	6,689	6,478
Cost of borrowed money.....	3,924	3,818	3,214	1,096	839
Depreciation, amortization and depletion.....	6,671	6,244	6,129	3,685	3,088
Net profit before income taxes.....	8,057	7,369	4,705	1,908	2,551
Provision for income taxes.....	3,980	3,590	1,570	1,249	—
Net profit for the year.....	4,077	3,779	3,135	659	2,551
Current assets:					
Cash and equivalent.....	4,275	6,899	9,084	3,662	4,077
Inventories.....	14,949	14,216	11,251	12,487	10,946
Other current.....	7,724	6,667	6,047	4,161	2,055
	26,948	27,782	26,382	20,310	17,078
Current liabilities.....	7,538	9,095	7,029	6,022	5,310
Working capital.....	19,410	18,687	19,353	14,288	11,768
Fixed assets at cost.....	138,510	130,450	123,185	118,347	107,584
Accumulated depreciation.....	40,893	36,381	31,286	26,509	22,582
Net fixed assets.....	97,617	94,069	91,899	91,838	85,002
Outstanding debt.....	61,742	61,742	61,742	44,439	35,242
Preferred shares (par value).....	5,000	5,000	7,500	25,000	25,000
Common equity.....	46,360	44,108	42,203	39,768	39,809



NORTHERN OPERATIONS

In all of the company's market areas, the demand for dissolving pulps remained very strong. North America continued to be the major consumer, but substantial shipments were also made to Japan and Europe. 160,000 tons, a record volume, were sold with sales being limited by plant output. A high proportion was in the more profitable acetate grades. There was a marked increase in the volume of pulp sold for triacetate end use and which is especially suited for the spinning of Arnel fibre. Progress was also recorded in the development of other pulp grades such as that used in the manufacture of cellulose nitrate lacquers.

Mill output, although the highest ever achieved, was only slightly greater than 1963. Delays were encountered in the completion of the project to expand production to the 530 tons per day level. The project included a new boiler, an extension to one of the three pulp drying machines, facilities to increase the volume of acid used in the pulping process and a new conveyor system to increase the supply of logs to the chip preparation plant. However, these facilities are now in operation and the resulting increased capacity is available. Mill output, therefore, should be substantially increased in 1965.

A one-year labour agreement, consistent with the industry pattern, was concluded. It provided a wage increase of 5% and fringe benefits.

Logging operations were active in all major areas of the Tree Farm and from that source some 247,000 cunits were produced. In the Nass area a large part of the supply was produced by contractors. Outside purchases of logs and chips totalled 147,000 cunits. A more competitive log market on the Coast resulted in an increase in prices for both logs and chips. Fire losses were at a minimum as a result of an unusually wet summer. At times logging efficiency was hampered



All these points have been connected to the main highway by Columbia Cellulose logging roads. Most of them lie within the boundary of T.F.L. No. 1.



Good roads and good equipment cost money, but their maintenance ensures a steady flow of logs to the mill. Here a truck at the Nass River is on its way to the booming ground.

by mud and flooding. The Alaska earthquake damaged some log rafts in storage, but a salvage programme with the help of aerial reconnaissance minimized losses. During the year long-range plans were developed for supplying wood to the expanded sulphite and the new kraft operations. In August the company was awarded Tree Farm Licence No. 40 in support of these expansions and some beneficial amendments were also made to the boundaries of Tree Farm Licence No. 1. Company foresters subsequently prepared working plans for these two areas. These plans will be the basis under which the company will operate during the next five years. Together the two Tree Farms will supply approximately two-thirds of the estimated annual requirements of 1,000,000 cunits. About one-third will be required as purchased logs and chips. During 1964 the Woods Division thoroughly investigated all outside sources of supply. Negotiations are being finalized whereby the company will acquire substantial supplies of pulp logs from these outside areas. With a view towards opening up the new area, the company accelerated its road and river development programme northwards in the Aiyansh Block and westerly on the south bank of the Nass River to tidewater. The development programme included the start of a headquarters in the Nass River area. Seven houses were built and occupied and provision made for trailer accommodation. A school was also built and is functioning.

Industry-wide negotiations involving the coast logging and sawmilling operations resulted in a two-year agreement to June 1966. As well as some fringe benefits, it provided for a 15¢ per hour wage increase in the first year and an additional 13¢ in the second year.

Forestry activities, which included cruising, surveys, reforestation and research were limited to maintenance of the current programme. Natural regeneration continues to be successful in the majority of cases. Approximately 500 acres required planting during the year.



Some customers want rolls, some want bales. Carefully wrapped against dirt and damage, Columbia Cellulose dissolving grades move by conveyor to the warehouse.

INTERIOR OPERATIONS

There was a strong demand for Celgar and other kraft pulps during the past year. In the fourth quarter of 1964 prices increased in the North American market and similar increases became effective as at January 1, 1965 for Europe. These levels should prevail throughout the coming year. Improvements at the Celgar pulp mill resulted in increased production of approximately 10,000 tons to a new high of 185,379 tons for the year. Some further improvement is planned.

Facilities are being installed to allow closer segregation of wood species to give the mill better control of quality.

The Celgar Lumber Division produced over 106 million feet of lumber in its first full year on a three-shift basis. Additional dry kiln capacity, now in excess of 70 million feet, was installed.

At the start of 1964 lumber prices were at a high level but from April onward there was a gradual decline. For the year, the average mill net was almost identical with 1963.

A three-year wage agreement was concluded, thus ensuring continuity of operation for this term in both sawmill and logging operations.

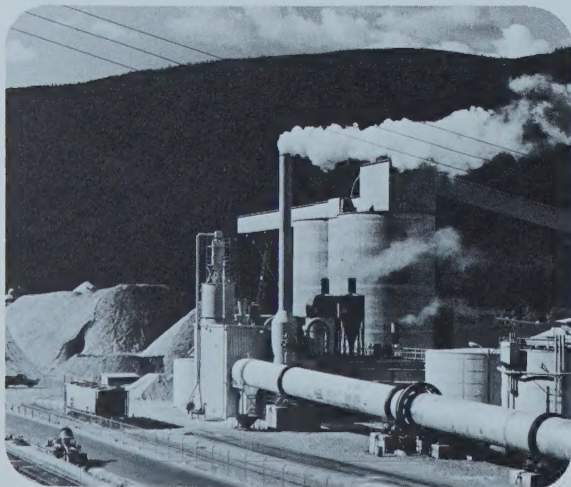
With the start of the Columbia River project, company personnel worked in close co-operation with the B.C. Hydro and Power Authority. The latter has undertaken to provide a new pipeline to carry clean water from the Lower Arrow Lake to the existing mill intake. The Authority will also provide for the movement of logs around the High Arrow Dam during the construction period.

Log production from the Tree Farm and adjoining Sustained Yield Units amounted to 411,000 cunits, of which 331,000 cunits were harvested on the Tree Farm. Of the latter total some 118,000 cunits were driven down the Columbia River from north of Revelstoke to the Upper Arrow Lake, in some instances up to a distance of 130 miles.

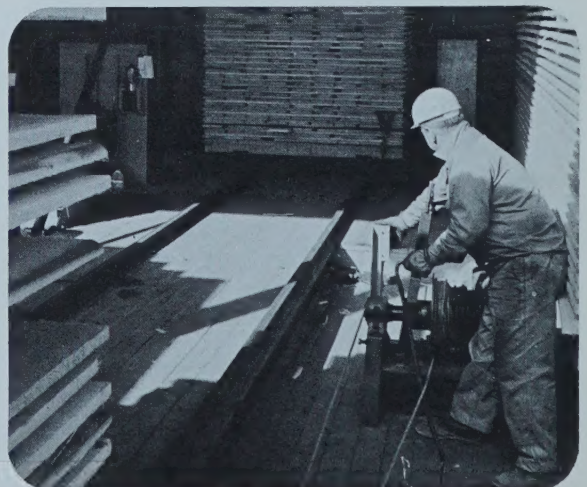
Development of the Tree Farm road system continued and was extended some 106 miles.

The occurrence and extent of fires were at a minimum as the fire hazard remained low throughout the season.

During the year a study of the integrated logging, lumber and pulp operations has been initiated. The study has used a linear programming technique with the aid of a computer. The results will guide future planning of the total wood resource to achieve optimum profits.



Distinguishing feature of a kraft pulp mill is the lime kiln and recausticizing plant. This huge rotating drum produces lime used in the cooking liquor.



Dry kilns remove the moisture from lumber so that it will not warp or check after it has been planed. Drying also reduces shipping charges.

RESEARCH & DEVELOPMENT

Plans for the establishment of the new research centre in Vancouver are proceeding, but as it will take several years to bring the new facilities into operation, temporary premises in the Annacis Industrial Estate have been obtained and now house the Research & Development Division.

In the past year a substantial part of the research activity was directed towards the Skeena Kraft project. A detailed examination was undertaken of the characteristics of the various wood species in the areas from which the new mill will draw its wood supplies. The data developed on fibre properties and on yields will enable optimum use of the wood in each manufacturing operation, kraft and sulphite. The work has also confirmed that the quality of the bleached kraft pulp from the new mill will be at least equivalent to the well accepted grades of Celgar Kraft.

Prince Rupert pulps are used mainly in the production of textile yarns and fibres. A part of the research effort is constantly directed in support of that market, and in that area, studies were active and aimed at extending existing knowledge of the relationship of specific pulp properties to yarn spinning stability and quality. In the development of new dissolving pulp grades, some progress was achieved. Throughout the year, the plant successfully produced small volumes of several modified grades. Here the research groups worked in close collaboration with operating personnel.

In support of the Celgar pulp mill, wood species evaluation was continued. To strengthen the future market position of this mill, special grades are being developed for specific end uses. In this connection process techniques for significantly modifying fibre properties are being investigated.



New products and new processes help to create new customers and broaden marketing opportunities. Research continues to play an important role in Columbia Cellulose's future.

SKEENA KRAFT LIMITED

During 1964 Skeena Kraft Limited was incorporated as a new company in British Columbia with 60% of the equity to be contributed by Columbia Cellulose Company, Limited and 40% by Svenska Cellulosa Aktiebolaget of Sundsvall, Sweden.

Skeena Kraft will commence construction of a 750-ton per day bleached kraft pulp mill in April, 1965 on a site adjacent to the existing Columbia Cellulose sulphite mill on Watson Island near Prince Rupert, British Columbia. The new mill will go on stream early in 1967 and is scheduled to reach full capacity in 1969. It will be the largest single-line operation which can be built with today's technology.

Integration of the facilities of the new kraft mill and the existing sulphite mill will enable sulphite capacity to be increased to 720 tons per day by 1971.

Capital investment for the overall project including construction, development of wood resources, working capital and expenditures on related facilities by Columbia Cellulose is \$79 million.

Wood resources have been secured in the form of 980,000 acres of newly allocated timber reserves held under Tree Farm Licence No. 40 with an estimated 33.2 million cunits of mature timber. Additional wood will be available from adjacent areas logged by independent operators.

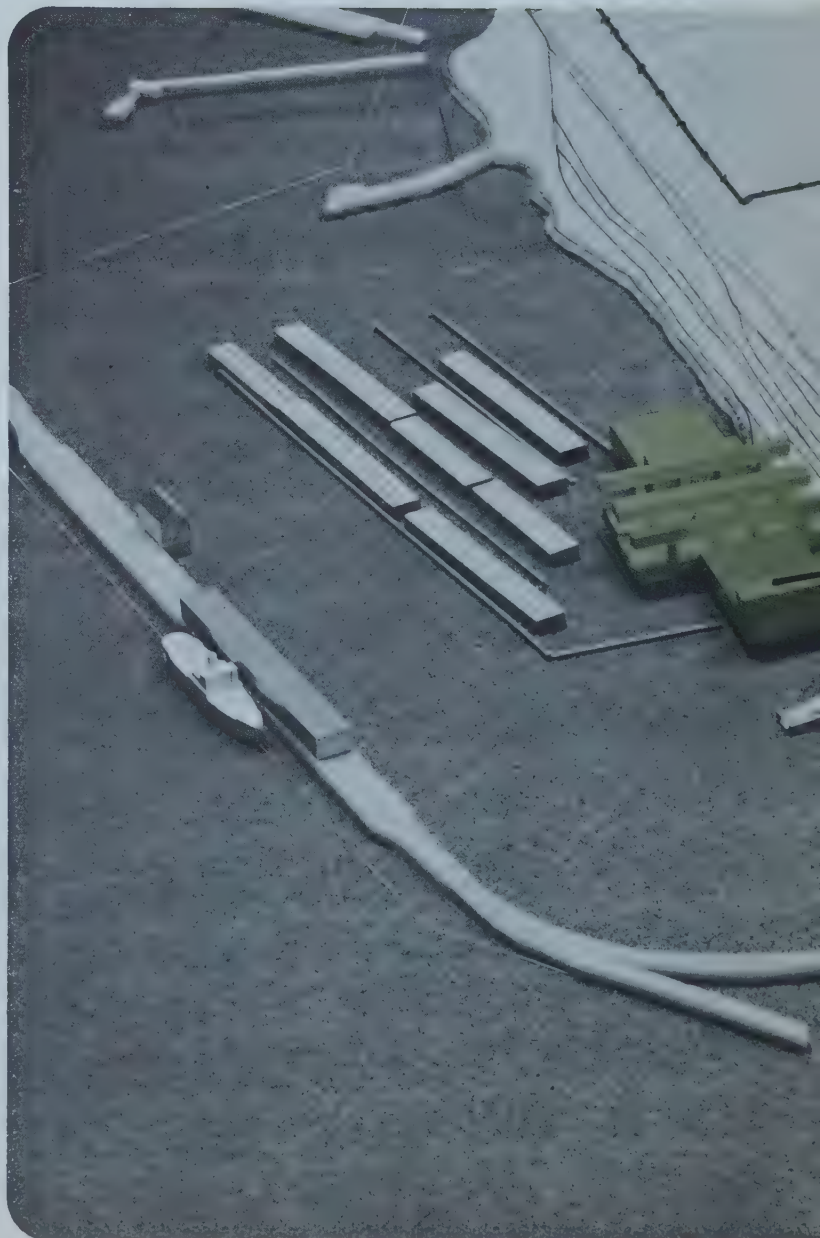
The main block of T.F.L. No. 40 is in the drainage area of the Upper Nass and Skeena Rivers north of T.F.L. No. 1 held by Columbia Cellulose. These two river systems will form the primary log transportation route to the mills.

Logging operations on T.F.L. No. 1 and T.F.L. No. 40 will be consolidated and carried out by a newly incorporated company owned equally by Columbia Cellulose and Skeena Kraft.

Integration of logging and manufacturing facilities in the two forest areas and the two mills will provide cost advantages and operating efficiencies to both Columbia Cellulose and Skeena Kraft and ensure better utilization of the total wood resources.

Adjacent to the mill site, Hooker Chemicals Limited will construct a chlorine and caustic plant, providing an economical chemical source for the Prince Rupert mills.

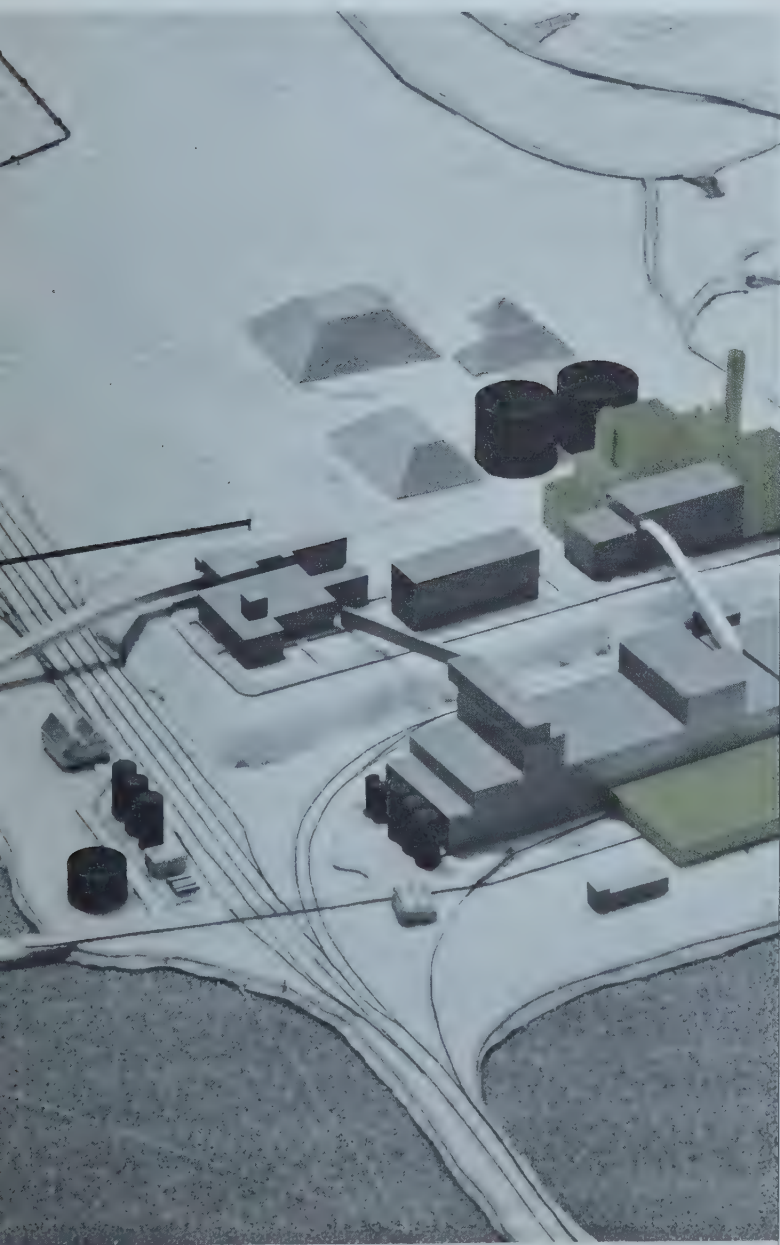
The worldwide marketing organizations of Columbia Cellulose and Svenska Cellulosa together provide powerful international sales coverage. The product from the new mill will be sold primarily in the growing European market, Japan, and North America, as well as the Far East and South America.



LEGEND

- T.F.L. No. 1 - Columbia Cellulose
- T.F.L. No. 40 - Skeena Kraft

Engineers use models to assist in mill layouts. This basic scale model is equipment units built in advance of construction to study design and avoid errors. Units shown in dark grey are dark; the new kraft mill is shown in green. Area outlined at upper left is plant to supply caustic and chlorine.



SVENSKA CELLULOSA AKTIEBOLAGET

Svenska Cellulosa is Sweden's largest integrated forest products producer and distributor. Although the company was formed in 1929 as a holding company for 16 subsidiary forest products organizations, many of these date back to the beginning of the 18th century.

Today S.C.A. is an integrated forest products and chemical company with headquarters in Sundsvall, Sweden. Its products include wood pulp, paper, lumber, fibreboard, manufactured wood products, plastics, plywood and chemicals including chlorine, sodium hydroxide and liquid resins. A subsidiary company manufactures industrial machinery and another produces hydro-electric power.

Sales are directed from Sundsvall and cover virtually the entire pulp and paper importing world. Offices and agents number twelve in Western Europe outside Scandinavia, eight in North and South America, eleven in Asia, nine in Africa and one in Australia. Scandinavian and Eastern European sales are made by the Sundsvall office. S.C.A. currently markets about 900,000 tons of paper and pulp annually of which about 525,000 tons are chemical pulp.

S.C.A. has been marketing pulp in the European market for nearly 50 years. The company has established an enviable reputation in sales and technical service.

Raw material scarcity is foreseen as the principal weakness in S.C.A.'s future development. In spite of a steady increase in wood production from its 3.5 million acres of productive timberland through intensive forestry, S.C.A. estimates that by 1967 the demands of its customers will outstrip the available wood supply.

This is the situation which has brought Columbia Cellulose and Svenska Cellulosa together in the new Skeena Kraft project.

If S.C.A. is to be able to meet the growing requirements of its customers and at the same time increase its paper production by 100% and expand its newsprint facilities as planned, pulp from the Skeena Kraft project is vital to its operations.

S.C.A. spends about \$2 million annually on the research and development activities that employ about 150 persons. This work has produced many notable advances in areas such as wood utilization, flash drying of pulp, pulp process modifications and heat and chemical recovery in the sulphite process.

This fine record of technological achievement, coupled with the local knowledge and operating experience of Columbia Cellulose in British Columbia, will produce an organization which will be a leader in technology and improved forest utilization.

LEGEND



T.F.L. No. 1 - Columbia Cellulose



T.F.L. No. 40 - Skeena Kraft

Engineers use models to assist in mill layouts. This basic scale model is supported by detailed replicas of major equipment units built in advance of construction to study design and avoid errors. Present sulphite mill buildings are dark; the new kraft mill is shown in green. Area outlined at upper left is site of proposed Hooker Chemical Limited plant to supply caustic and chlorine.



MANUFACTURING PROCESSES

What is the difference between sulphite and sulphate pulp? How do you make pulp? These are questions asked by many people – even those working in the forest industries. This brief explanation may contribute to a better understanding of our Columbia Cellulose operations.

Wood is comprised of long, hollow tubes known as cells or fibres. These are bonded together by a dark substance called lignin. Chemical pulping processes attempt to dissolve the lignin without destroying the cellulose fibres which are valuable as chemicals or for use in papermaking.

The two most successful chemical pulping processes are called sulphite and sulphate. Another name for the sulphate process is the "kraft" process. The process got this name because the sulphate process yields strong fibres and the German word for "strength" is "kraft".

The distinguishing feature of the two processes is the composition of the chemical cooking liquor. The sulphite process uses an acid and the sulphate, or kraft process, uses an alkaline liquor.

To make calcium bi-sulphite, the acid liquor, sulphur dioxide gas passes up through a tower of limestone rock while water trickles down. The cold water absorbs the gas and produces a chemical reaction with the limestone, yielding the acid cooking solution, calcium bi-sulphite.

Similarly the kraft process produces an alkaline cooking liquor which resembles a solution of household lye. However, one of the economies of the kraft process is its ability to recover heat and chemicals in a three-stage cycle of cooking, chemical recovery and liquor-making. The active ingredients in the cooking liquor are sodium hydroxide and sodium sulphide. During cooking, pulp and "black liquor" (containing the dissolved non-cellulosic materials) are produced. Water is evaporated from the liquor, and the mixture burned to produce steam. The chemicals form slag and fall to the bottom of the furnace. This slag is dissolved in water to form what is called "green liquor". Reclaimed sludge and fresh limestone are burned in a long, revolving kiln, and the lime produced is added to the "green liquor" to complete the cycle by making fresh "white liquor" for the digesters.

Except in their chemical processes, sulphite and kraft mills are similar.

The kraft process is able to make use of a wider range of wood species than the sulphite process, and therefore can make fuller use of the forest and of sawmill waste.

The Prince Rupert sulphite mill of Columbia Cellulose makes an extremely pure pulp for textiles, plastics and chemicals. The bleaching and purification stages are, therefore, much more exacting than in most other mills.



SOURCE AND APPLICATION OF FUNDS

(in thousands of dollars)

SOURCE OF FUNDS:	1964	1963
Funds provided by operations:		
Net profit for the year.....	\$ 4,077	3,779
Provision for depreciation and other non-cash charges.....	6,671	6,244
Provision for future income taxes.....	2,127	1,660
Net funds provided by operations.....	<u>12,875</u>	<u>11,683</u>
Funds provided by capital changes:		
Redemption of preferred shares.....	—	(2,500)
Net funds provided by capital changes.....	—	<u>(2,500)</u>
NET FUNDS PROVIDED.....	12,875	9,183
APPLICATION OF FUNDS:		
Capital expenditures – net cash outlay.....	9,649	8,185
Preliminary expenditure on new pulp mill project.....	585	—
Dividends paid.....	1,831	1,874
Increase in receivables, inventories, prepayments, etc., less change in payables and accrued items.....	3,427	1,302
Others.....	7	7
NET FUNDS APPLIED.....	15,499	11,368
EXCESS OF FUNDS APPLIED OVER FUNDS PROVIDED.....	2,624	2,185
OPENING BALANCE OF CASH AND EQUIVALENT.....	6,899	9,084
CLOSING BALANCE OF CASH AND EQUIVALENT.....	<u>\$ 4,275</u>	<u>6,899</u>

CONSOLIDATED STATEMENT OF EARNINGS

for the year ended December 31, 1964 with 1963 comparison

	1964	1963
Net sales.....	\$62,347,417	56,768,023
Cost of goods sold.....	40,983,138	36,691,811
Selling, administrative and research expenses.....	2,711,850	2,644,815
	<u>43,694,988</u>	<u>39,336,626</u>
Operating profit before depreciation.....	<u>18,652,429</u>	<u>17,431,397</u>
Other charges:		
Interest on mortgage bonds.....	3,962,684	3,966,060
Other interest expense.....	23,157	19,729
	<u>3,985,841</u>	<u>3,985,789</u>
Less interest income.....	<u>62,169</u>	<u>168,188</u>
	<u>3,923,672</u>	<u>3,817,601</u>
Net profit before the undernoted provisions.....	<u>14,728,757</u>	<u>13,613,796</u>
Depreciation, amortization and depletion.....	6,241,253	5,814,211
Amortization of mill start-up expenses.....	361,852	361,852
Amortization of financing costs.....	68,274	68,275
	<u>6,671,379</u>	<u>6,244,338</u>
Net profit before income taxes.....	<u>8,057,378</u>	<u>7,369,458</u>
Provision for income taxes (Note 5).....	<u>3,980,000</u>	<u>3,590,000</u>
Net profit for the year.....	<u>\$ 4,077,378</u>	<u>3,779,458</u>

CONSOLIDATED STATEMENT OF SURPLUS

for the year ended December 31, 1964 with 1963 comparison

	1964	1963
Surplus at beginning of year.....	\$ 9,758,396	7,853,288
Net profit for the year.....	4,077,378	3,779,458
	<u>13,835,774</u>	<u>11,632,746</u>
Dividends:		
Preferred shares.....	350,000	393,750
Common shares.....	1,480,761	1,480,600
	<u>1,830,761</u>	<u>1,874,350</u>
Surplus at end of year (Note 4).....	<u>\$12,005,013</u>	<u>9,758,396</u>

See accompanying notes to consolidated financial statements.



CONSOLIDATED

December 31, 196

ASSETS

CURRENT ASSETS:	1964	1963
Cash.....	\$ 4,274,970	6,898,629
Accounts receivable:		
Trade and other.....	7,539,880	6,411,238
Affiliate.....	8,592	133,562
Inventories (Note 2).....	14,949,395	14,216,087
Insurance and other payments in advance.....	175,409	122,451
Total current assets.....	<u>26,948,246</u>	<u>27,781,967</u>
 EMPLOYEE MORTGAGES, DEPOSITS AND PROPERTY FOR DISPOSAL.....	 672,936	 610,069
 FIXED ASSETS, AT COST:		
Land.....	449,087	424,621
Timber licences, roads and related facilities.....	15,758,799	14,502,723
Buildings, machinery and equipment.....	122,301,942	115,522,516
	<u>138,509,828</u>	<u>130,449,860</u>
Less accumulated depreciation, amortization and depletion....	40,892,956	36,380,468
	<u>97,616,872</u>	<u>94,069,392</u>
 PRELIMINARY EXPENDITURE ON NEW PULP MILL PROJECT (Note 3).....	 585,574	 —
 DEFERRED CHARGES, LESS AMOUNTS WRITTEN OFF:		
Mill start-up expenses.....	633,235	995,087
Timber reconnaissance.....	675,788	836,147
Financing expenses.....	136,547	204,821
	<u>1,445,570</u>	<u>2,036,055</u>
	<u>\$127,269,198</u>	<u>124,497,483</u>

See accompanying notes to consolidated financial statements.

BALANCE SHEET

with 1963 comparison

LIABILITIES

CURRENT LIABILITIES:	1964	1963
Accounts payable and accrued liabilities.....\$	4,788,242	5,172,827
Accrued bond interest.....	1,973,590	1,986,153
Income taxes payable.....	775,876	1,936,430
Total current liabilities.....	7,537,708	9,095,410

OTHER LIABILITIES:

6½% First Mortgage 20-year bonds due January 2, 1981 (Note 4).....	61,742,183	61,742,183
Timber licence purchase agreement.....	50,000	100,000
	61,792,183	61,842,183
RESERVE FOR FUTURE INCOME TAXES (Note 5).....	6,579,000	4,452,000

SHAREHOLDERS' EQUITY (Notes 4 and 6):

Capital stock:

7% cumulative redeemable preferred shares of \$2 each. Authorized and issued 5,000,000 shares, less redeemed 2,500,000 shares; is- sued and outstanding 2,500,000 shares.....	5,000,000	5,000,000
Common shares of no par value. Authorized 10,000,000 shares; issued 7,403,803 shares.....	34,355,294	34,349,494
Surplus, per accompanying statement.....	12,005,013	9,758,396
	51,360,307	49,107,890

COMMITMENTS (Notes 3 and 7)

\$127,269,198	124,497,483
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Signed on behalf of the Board:
M. W. MACKENZIE, *Director*.
PAUL M. MARSHALL, *Director*.



NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 1964

1. **CONVERSION OF FOREIGN CURRENCIES:** Current assets and current liabilities in foreign currencies have been converted into Canadian dollars at the rates of exchange in effect at December 31, 1964. The mortgage bonds payable in U.S. funds have been converted at rates established at the time of receipt of the funds secured under the bonds.

2. **INVENTORIES:** Inventories at December 31, 1964, were valued at average cost or less, and were not in excess of market. A summary of the inventories is as follows:

Raw materials.....	\$11,167,596
Work in process.....	22,966
Finished goods.....	602,075
Stores and supplies.....	3,156,758
	<u>\$14,949,395</u>

3. **PRELIMINARY EXPENDITURE ON NEW PULP MILL PROJECT:** The company has formed a joint venture with Svenska Cellulosa Aktiebolaget of Sweden, whereby a newly incorporated company, Skeena Kraft Limited, will construct a kraft pulp mill integrated with the company's Prince Rupert mill. The new company will be 60% owned by Columbia Cellulose and 40% by Svenska Cellulosa Aktiebolaget. The total cost including woods operations and working capital is estimated at \$67,000,000 of which the company's contribution will be approximately \$15,000,000. At December 31, 1964, preliminary expenses incurred on this project were \$585,574, and commitments with respect to construction amounted to approximately \$6,700,000. These amounts will be charged to Skeena Kraft Limited in 1965.

In addition, the company is planning expenditures of some \$12,000,000 to increase its basic utilities which will, in part, serve Skeena Kraft Limited, and also make possible a future expansion of the existing sulphite mill.

4. **6½% FIRST MORTGAGE 20-YEAR BONDS:** A wholly-owned subsidiary, Celgar Limited, has issued U.S. \$60,000,000 6½% first mortgage 20-year bonds due January 2, 1981, with an annual sinking fund requirement from 1967 to 1980, inclusive, of U.S. \$4,000,000. The bonds are secured by a fixed and floating charge on the assets of Celgar Limited, the net book value of which at December 31, 1964 amounted to \$126,261,534. Among other things, the terms of the trust deed securing the bonds provide that Celgar Limited will not declare or pay dividends, other than stock dividends, or reduce its capital stock except to the extent of 80% of its consolidated net profit from January 1, 1961. The effect of this restriction at December 31, 1964 is to limit to \$10,392,319 the amount of consolidated surplus of Columbia Cellulose Company, Limited at that date, which may be applied to the payment of dividends by that company.

Columbia Cellulose Company, Limited guarantees the payment of any sums which may become due from Celgar Limited under the terms of the trust deed securing the bonds.

5. **INCOME TAXES:** It is expected that depreciation for tax purposes will be claimed in 1964 in excess of that recorded in the accounts and accordingly the amount provided for income taxes in the consolidated statement of earnings includes \$2,127,000 for income taxes that would otherwise have been payable. This amount is included in "Reserve for future income taxes" in the balance sheet. In future years when the depreciation recorded in the accounts may exceed that allowable for tax purposes, the tax on those excess amounts would be charged against the reserve and not against the income of those years.

6. **CAPITAL STOCK:** On April 6, 1964, the 7% cumulative redeemable preferred shares were subdivided from a par value of \$100 per share to \$2 per share; accordingly, the authorized and issued preferred share capital became 5,000,000 preferred shares and 2,500,000 preferred shares respectively. The preferred shares are redeemable in whole or in part at the option of the company at any time at par, plus accrued dividends; once redeemed the shares cannot be re-issued.

Under a stock option plan adopted in April 1963, 100,000 common shares were reserved for issue to officers and employees. Options on 45,400 common shares have been issued at the market price at date of issue, \$7.25 per share. The options, which expire December 31, 1973, are exercisable as to 20% a year on a cumulative basis from April 19, 1964. Options on 800 shares have been exercised to December 31, 1964.

7. **COMMITMENTS:** At December 31, 1964, capital commitments amounted to approximately \$3,170,000 in addition to the commitments referred to in Note 3.

8. **SELLING, ADMINISTRATIVE AND RESEARCH EXPENSES:** Directors' fees for the year ended December 31, 1964 amounted to \$32,850.

AUDITORS' REPORT TO THE SHAREHOLDERS

We have examined the consolidated balance sheet of Columbia Cellulose Company, Limited and its subsidiary companies as of December 31, 1964 and the consolidated statements of earnings and surplus for the year ended on that date and have obtained all the information and explanations we have required. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion, and according to the best of our information and the explanations given to us and as shown by the books of the companies, the accompanying consolidated balance sheet and related consolidated statements of earnings and surplus are properly drawn up so as to exhibit a true and correct view of the state of the affairs of the companies on a consolidated basis at December 31, 1964 and the results of their operations for the year ended on that date, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Vancouver, B.C., January 27, 1965

PEAT, MARWICK, MITCHELL & CO., Chartered Accountants.

OUTLOOK

Demand for the sulphite and sulphate grades of pulp produced by the company has been very strong during the past year. Price increases were initiated in the North American market during the year and similar increases in overseas markets will be instituted early in 1965. There is every indication that both dissolving and bleached kraft pulps will continue to be in tight supply during the coming year.

The announcement of new kraft pulp mills by North American companies has been the rule rather than the exception during the past year. The resulting tonnage that will be available to pulp consumers during the years 1967 to 1971 is indeed formidable. All available forecasts, however, show free-world demand for bleached kraft pulps exceeding supply by 1971. Dependent upon the timing of the completion of some of the pulp mill construction projects now in the planning stage, there could be some excess capacity.

The very extensive increase in both supply and demand of bleached kraft pulps that confronts our industry at the present time highlights the importance of sound marketing in the years ahead. Those companies whose new product is consumed internally by their own integrated facilities and those with the broadest and most penetrating marketing organizations will undoubtedly be in the best position to benefit to the full from the expanding demand. The association of our company's world-wide marketing organization with that of our Skeena partner, Svenska Cellulosa Aktiebolaget, Sweden's largest distributor of forest products, augurs well for the success of our new venture.

With markets for all the company's products remaining firm, prices somewhat higher than those prevailing last year and increased capacity available at both mills, both sales and profits for 1965 should show improvement over 1964. However, extremely heavy snows in the Prince Rupert area and unusually cold weather in the interior of the province have severely restricted all production operations of the company during the first few weeks of the year. This will have an adverse effect on profits for the first quarter, but prospects for the remainder of the year appear bright.



Stereoscopic aerial photographs assist foresters to make detailed timber inventories quickly, accurately and economically right in their offices.

FOREST TO PRODUCT

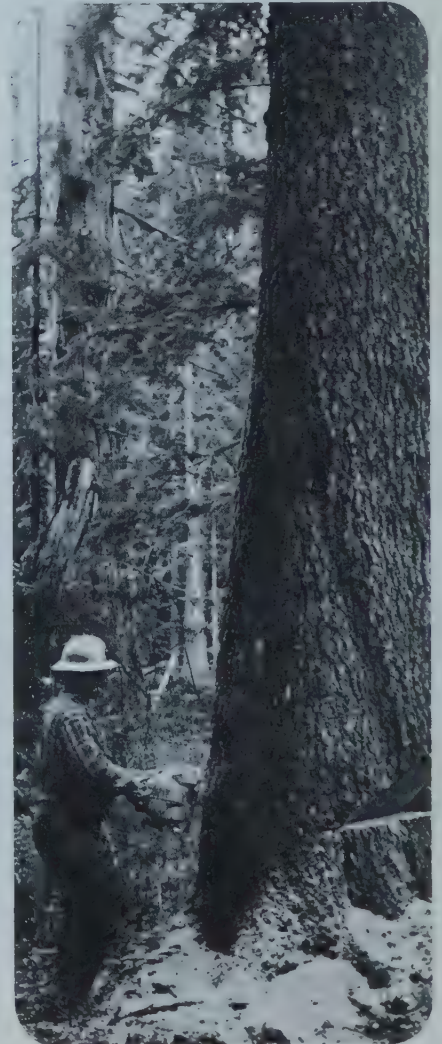
In British Columbia planned logging usually ensures that the forests regenerate themselves by natural seeding. Where nature fails, Columbia Cellulose is ready to plant seedlings from its tree nurseries. Hybrid poplar cuttings are also cultivated to plant in rich bottom lands. Moist climatic conditions maintain a good growing season. The forest management plan ensures that this renewable timber resource will give permanence to company operations.



Engineering and scientific technology are brought together in the pulp manufacturing process and in the subsequent processes of the textile, plastics, chemical and papermaking industries to create a myriad of wonderful products from the forest.



Seed blocks provide for natural forest regrowth.



BOARD OF DIRECTORS

HAROLD BLANCKE	G. W. GRANT McCONACHIE
A. R. COCHRAN	EDWIN C. McDONALD
R. W. KIXMILLER	ROBINSON ORD
C. J. MACKENZIE	HON. JAMES SINCLAIR
M. W. MACKENZIE	R. E. STAVERT
PAUL M. MARSHALL	R. L. WELDON

CORPORATE OFFICERS

M. W. MACKENZIE, *Chairman of the Board*
PAUL M. MARSHALL, *President*
A. E. PENNEY, *Executive Vice-President*
C. B. DUNHAM, *Vice-President, Forest Operations*
EUGENE DeLUCA, *Vice-President, Manufacturing and Engineering*
F. E. HERTHA, *Treasurer*
STEWART ROUTLEDGE, *Secretary and Assistant Treasurer*
G. M. GREER, *Assistant Secretary*
W. G. HOMENUK, *Comptroller*

OTHER SENIOR OPERATING OFFICERS

CLEMENT GARSIDE, *General Manager, Pulp and Lumber – Interior Operations*
W. E. D. GRAY, *General Manager, Columbia Pulp Sales*
L. S. MCGILL, *Director of Administration*
D. R. MUIR, *Director of Research and Development*
D. W. BROOKES, *Manager, Celgar Lumber Division*
I. A. CAIRNS, *Manager, Celgar Pulp Division*
R. R. JORDAN, *Manager, Celgar Woods Division*
W. D. STOTHERT, *Manager, Prince Rupert Pulp Division*
R. C. TELFORD, *Manager, Terrace Woods Division*

TRANSFER AGENTS

MONTREAL TRUST COMPANY, *Vancouver, Toronto, Montreal*
BANKERS TRUST COMPANY, *New York*

REGISTRARS

THE ROYAL TRUST COMPANY, *Vancouver, Toronto, Montreal*
THE CHASE MANHATTAN BANK, *New York*

STOCK LISTINGS

VANCOUVER, TORONTO AND MONTREAL STOCK EXCHANGES

AUDITORS

PEAT, MARWICK, MITCHELL & CO., *Vancouver*

ANNUAL MEETING

FRIDAY, FEBRUARY 26, 1965 – *Vancouver*

